Can anyone stop Wal-Mart?

June 22, 1992 Four Dollars

# Forbes

# MONEY GUIDE

**Wrap accounts: Just say no**
**Life insurance for high risks**
**Beat the IRS anti-hobby rules**
**Retirement strategies**
**An undiscovered small-cap fund**
**Which Japanese stocks to buy now**
**What to do with a busted tax shelter**
**Restructuring your personal balance sheet**

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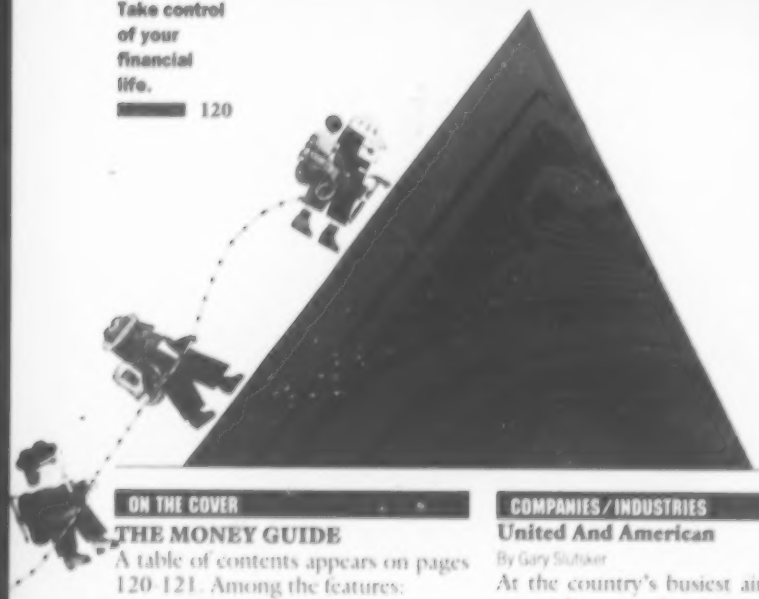

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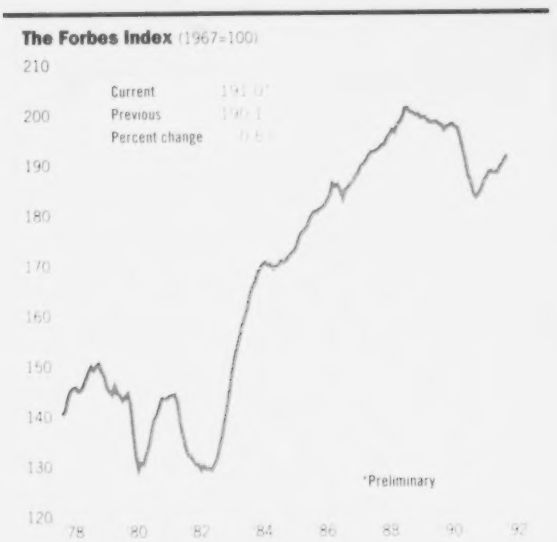
# THE FORBES INDEX

BY TIMOTHY DODMAN




The economy is doing better than we thought. The first of two scheduled revisions by the Commerce Department in the gross domestic product puts annualized growth in the first quarter at 2.4%, as opposed to the original estimate of 2%. Personal spending climbed, net of inflation, at a 5.4% annual rate in the first quarter. The second quarter seems to have gotten off to a good start. Manufacturers' new orders in April rose 1.4%. A high installment credit number (to be reported June 5) could put the Forbes Index for April at its highest level since November 1990.

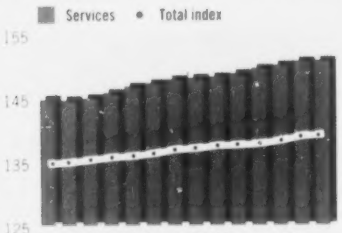
| Other key rates | Source | Status |
|---|---|---|
| Prime rate | Chase Manhattan Bank | 6.5% |
| Auto sales year to date vs 1991[1] | Ward's Automotive | 2.4% |
| Index of leading indicators Mar vs Feb | Dept of Commerce | 0.2% |
| Trade balance 12 months ended Mar 1992 | Dept of Commerce | -$68 bil |
| All-commodity producer price index Apr vs Mar[2] | Dept of Labor | 0.2% |
| GDP 1st quarter vs 4th—annualized growth | Dept of Commerce | 2.4% |
| M2 (3-month change)—annualized growth[3] | Federal Reserve | 2.7% |

[1] U.S.-based manufacturers, excludes imports, as of 5/20/92. [2] Wholesale goods. [3] Includes M1 (public currency and checking deposits) plus savings accounts and money market funds.

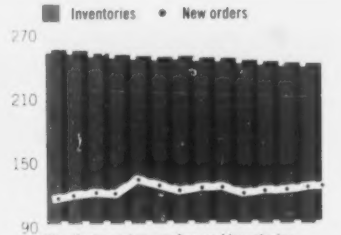
## Index components

The Forbes Index is a measure of U.S. economic activity composed of 8 equally weighted elements. Total industrial production, new claims for unemployment compensation, the cost of services relative to all consumer prices, new housing starts, total retail sales, the level of new orders for durable goods compared with manufacturers' inventories, personal income, total consumer installment credit.

To measure those 8 elements, Forbes consolidates 10 series of U.S. government data. The last 24 months' data for each series are presented below.



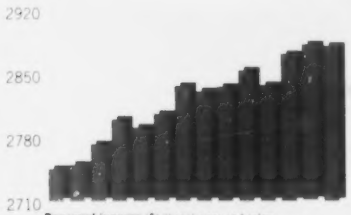

**Consumer price indexes** (1982-84 average=100) all urban consumers, unadjusted (Dept of Labor)



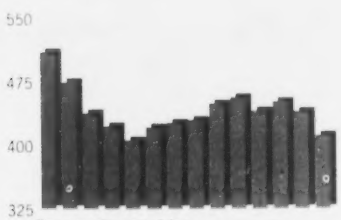

**Manufacturers' new orders and inventories** ($billions), seasonally adjusted (Dept of Commerce)

**Industrial production index** (1987=100) seasonally adjusted (Federal Reserve)

**New housing starts** (thousands) privately owned, unadjusted (Dept of Commerce)




**Personal income** ($billions) wage and salary disbursements, seasonally adjusted (Dept of Commerce)




**New unemployment claims** average for month (thousands), seasonally adjusted (Dept of Labor)

**Retail sales** ($billions), seasonally adjusted (Dept of Commerce)

**Consumer installment credit** ($billions) total, seasonally adjusted (Federal Reserve)

M A M J J A S O N D J F M A M A M J J A S O N D J F M A M A M J J A S O N D J F M A

If you want to make money in IPOs here are two solid pieces of advice: Stick with the largest underwriters and buy in the slowest years.

# New issue roulette

**By Warren Midgett and Scott DeCarlo**

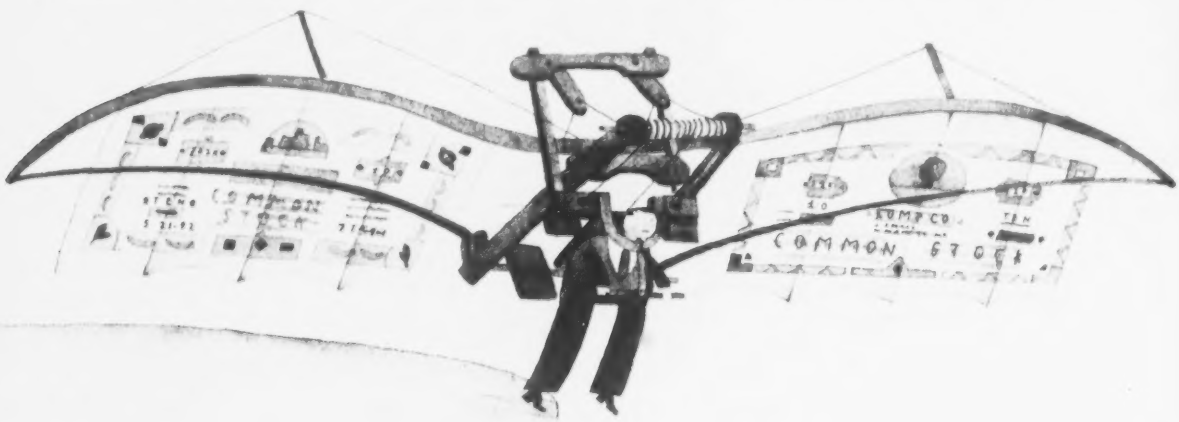
THERE'S no denying the siren song of the new issues market. All of us look back and wish that we had invested in Microsoft when it first came public in early 1986. A $10,000 investment made then is worth $315,000 now.

In boom years like 1991-92 people lucky enough to get allotments of hot new issues can often turn a fast profit. But as investments, as opposed to fast speculations, initial public offerings don't have a lot to recommend them. The harsh reality is that only one new issue in a thousand fares as well as Microsoft. Half of all the new issues that came out over the past decade have gone down—in a very bullish market. Almost two-thirds of them have done worse than the stock market as a whole.

FORBES tracked down 2,444 companies that went public since the beginning of 1982. We scored a stock as 100 if its performance tracked the market from issue date to Apr. 30, 1992. More precisely, relative-to-market performance is calculated by dividing the ending value of $100 invested in a new issue by the ending value of $1 invested in the S&P 500. Thus, 110 means that a buyer ended up 10% better off than he would have been if he had bought the S&P 500 index on the same date.

There were some big winners—Microsoft, US HealthCare, American Power Conversion. But the story is told in the averages. The average relative performance score for the past decade of initial public offerings: a dismal 95.

"I don't think a dealer in a Vegas casino is equally as equipped to stack the cards against you as the management and underwriter of an IPO. If the odds could be properly calculated, the game would be declared illegal," says G. Kenneth Heebner, manager of the TNE Growth Fund. Heebner has steered this fund onto the FORBES



## Get 'em when they're cold

| Year | Number of issues | Performance* actual | Performance* rel to S&P 500 | Performance* rel to Nasdaq |
|---|---|---|---|---|
| 1982 | 43 | 207.6% | 118 | 136 |
| 1983 | 443 | 59.0 | 75 | 94 |
| 1984 | 165 | 81.4 | 86 | 96 |
| 1985 | 189 | 68.9 | 88 | 98 |
| 1986 | 464 | 42.3 | 89 | 100 |
| 1987 | 344 | 24.7 | 95 | 98 |
| 1988 | 123 | 83.8 | 121 | 124 |
| 1989 | 116 | 59.8 | 128 | 124 |
| 1990 | 112 | 17.7 | 98 | 88 |
| 1991 | 266 | 24.7 | 114 | 109 |
| 1992* | 537† | -2.5 | 97 | 105 |
| Average | | 47.1 | 95 | 102 |

*Through Apr. 30. †Annualized

**The best vintage for new issues in the past decade was 1989, a very slow year. The worst was effervescent 1983, when 443 companies went public. It won't be surprising if 1992 is a poor year.**

mutual fund honor roll for seven consecutive years by investing in blue-chip companies with strong growth records. The only recent new issue in Heebner's portfolio is Duracell International.

Our scores, moreover, are too kind to the new issues business in two ways. First, we assumed that any buyer could have had any new issue at the offering price. The reality is otherwise. The most desirable new issues disappear into the hands of the underwriter's most loyal institutional customers, and the general public is left to buy shares at a premium in the aftermarket (FORBES, *May 25*).

Associate Professor Jay Ritter of the University of Illinois at Urbana-Champaign has reduced this hot-issue phenomenon to numbers. Ritter studied 8,668 new issues from 1960 to 1987 and found that they rose an average 8.6% in the first day of trading. (That's with low-priced penny stocks excluded; include them and the first-day jump is considerably higher.) In short, if you aren't lucky enough to be cut in at the offering price, you have to buy in the aftermarket and pay 8% more.

Second, we ignored dividends, which added an average of 4 percentage points a year to the performance of the S&P 500 but next to nothing to new issues.

In short, our latest findings reinforce what FORBES has been saying ever since it created the new issues database *(Dec. 2, 1985)*: Initial public offerings tend to enrich insiders and underwriters much more than they enrich the typical brokerage customer.

But our research turns up a few ways to improve your odds a bit. One lesson is that the biggest underwriters do better than the smallest. (The latter group includes self-underwriters—companies that sell shares without the help of a Wall Street firm.) The table below shows the average scores for the ten biggest lead underwriters. The 961 new issues whose lead manager was among these ten firms have an average relative performance score of 101.

What about the 1,483 stocks that were not underwritten by one of the top ten brokerage houses? This group rang up an average relative performance of only 90. Within this smaller-underwriter group, some well-known second-tier firms really bombed. Over the past decade Advest, a regional brokerage based in Hartford, took to market 25 issues that delivered a sorry-looking score of 62. The 59 issues underwritten by L.F. Rothschild (now defunct) have a relative performance of 67.

So if you want to play the new issue game, start your hunt with the larger sponsors, especially the ones with the best records. Goldman, Sachs is credited with taking more than $10 billion worth of stock to market, and it also shows the best score, 133, of the biggest investment bankers. Among its winners: Microsoft, Tyco Toys and Legent.

Next, there is a clear correlation between scarcity and value. The three years with the best crops of new issues—1988, 1989 and 1982—were all years when the deals were coming

## The biggest underwriters

| Underwriter | Number of issues | % of issues that went up | % of issues that beat the market | Average performance actual | Average performance rel to S&P 500 | Total offer val ($mil) |
|---|---|---|---|---|---|---|
| Goldman Sachs | 100 | 66% | 50% | 102% | 133 | $10,399 |
| Merrill Lynch | 152 | 49 | 36 | 55 | 97 | 8,592 |
| Morgan Stanley | 86 | 62 | 47 | 55 | 109 | 5,611 |
| First Boston | 66 | 62 | 45 | 30 | 99 | 4,567 |
| Shearson Lehman Brothers | 70 | 53 | 41 | 60 | 104 | 4,305 |
| Salomon Brothers | 55 | 65 | 38 | 42 | 87 | 4,099 |
| Drexel Burnham Lambert* | 113 | 48 | 30 | 51 | 93 | 3,643 |
| Alex Brown & Sons | 140 | 59 | 46 | 58 | 111 | 3,451 |
| Kidder Peabody | 91 | 41 | 32 | 30 | 86 | 2,773 |
| PaineWebber | 88 | 45 | 31 | 46 | 94 | 2,621 |

*Bankrupt.

**Some underwriters price their deals low enough to give the investor a fighting chance; others do not. To improve your odds, buy from underwriters with the best performance relative to the market.**

## The top-performing new issues

| Company/business | Price offer[1] | Price recent[2] | Offer value (mil) | Offer date | gain actual | gain rel to S&P 500[3] | Underwriter |
|---|---|---|---|---|---|---|---|
| **US HealthCare**/health care services | $1.17 | $49.50 | $20 | 2/11/83 | 4,131% | 1,505 | Merrill Lynch |
| **Microsoft**/computer software | 3.50 | 110.25 | 59 | 3/14/86 | 3,049 | 1,795 | Goldman Sachs |
| **Atlantic Southeast Air**/airline | 1.08 | 31.75 | 5 | 12/28/82 | 2,829 | 999 | Robinson-Humphrey |
| **Amer Power Conv**/back-up batteries | 1.00 | 28.25 | 6 | 7/29/88 | 2,725 | 1,852 | Josephthal |
| **Washington Federal S&L**/thrift | 1.06 | 26.38 | 11 | 1/17/83 | 2,398 | 886 | EF Hutton[4] |
| **King World Productions**/entertainment | 1.11 | 25.38 | 13 | 12/7/84 | 2,184 | 893 | PaineWebber |
| **Conseco**/insurance | 1.75 | 33.00 | 7 | 11/15/85 | 1,786 | 900 | Laidlaw Adams & Peck |
| **Amgen**/biotechnology | 3.00 | 56.00 | 42 | 6/30/83 | 1,766 | 756 | Smith Barney |
| **Surgical Care Affiliates**/health care svcs | 1.99 | 32.25 | 14 | 1/18/84 | 1,520 | 654 | Ladenburg Thalmann |
| **Adobe Systems**/computer software | 2.75 | 44.25 | 6 | 8/15/86 | 1,509 | 958 | Hambrecht & Quist |

## The worst-performing new issues

| Company/business | Price offer[1] | Price recent[2] | Offer value ($mil) | Offer date | Underwriter |
|---|---|---|---|---|---|
| **Tigera Group**[5]/computer software | $22.00 | $0.25 | $110 | 3/31/83 | First Boston |
| **Worlds Of Wonder**[6]/toys | 18.00 | 0.00 | 108 | 6/20/86 | Smith Barney |
| **CrossLand Savings**/thrifts | 9.00 | 0.02 | 100 | 10/25/85 | Salomon Brothers |
| **Goldome**/thrifts | 7.00 | 0.00 | 98 | 8/11/87 | Merrill Lynch |
| **Victor Technologies**/computer equipment | 280.00 | 0.38[7] | 79 | 3/31/83 | LF Rothschild[8] |
| **Inovision**[9]/entertainment | 13.00 | 0.01 | 70 | 10/11/85 | Merrill Lynch |
| **General Homes**[6]/building | 19.00 | 0.00 | 67 | 6/30/83 | Shearson Lehman |
| **Priam**[6]/computer equipment | 17.00 | 0.03[7] | 65 | 6/21/83 | Hambrecht & Quist |
| **Elxsi**[10]/financial services | 12.00 | 0.22 | 60 | 11/10/83 | Merrill Lynch |
| **AmeriFirst Bank**/thrifts | 8.00 | 0.00 | 57 | 11/7/86 | PaineWebber |

[1]Per common share adjusted for splits. [2]As of Apr. 30. [3]Ending value of $100 invested in the stock divided by $1 invested in the S&P 500. [4]Now part of Shearson Lehman Brothers. [5]Formerly Fortune Systems. [6]Bankrupt. [7]Most recent quote available. [8]Now defunct. [9]Formerly Vestron. [10]Formerly Trilogy Ltd. *Sources: Security Data Co.; Wilshire Associates; Forbes.*

**One of the biggest initial public offerings of the decade, the $59 million Microsoft deal was a bonanza for investors. But plenty of other offerings bombed. The largest of them are shown at left.**

out at a rate of less than three per week. Busy years like 1983 and 1986, in contrast, tended to be very bad for investors.

It stands to reason. When the market is high and the demand for new issues is insatiable, underwriters reach down into the bottom of the barrel for material, and they price it richly. But when no one wants to buy stocks, the dealmakers offer only their best candidates, and offer them at attractive prices.

It's a little early to see how well the class of 1992 will fare, but the dizzying volume at which new issues are coming to market these days is surely a bad sign. This year, through Apr. 30, there were 179 new issues, raising nearly $10 billion in capital. Annualize these numbers and you are looking at record highs: 537 issues raising $30 billion. In contrast, from 1988 through 1990 only 351 new issues were taken to market and $12.6 billion was raised.

Biotechnology stocks have been particularly hot. This sector accounts for 15% of the number of issues that came public in 1991 and 19% of the new offerings through April of this year. But, following a sharp setback in April, almost 90% of the biotechnology stocks offered this year have shown negative performances since they came out, according to Securities Data Co. Warns Evan Sturza, of *Sturza's Medical Investment Letter:* "Maybe a lesson was learned that you shouldn't buy IPOs. There have been too many biotech IPOs in the last two years—about 200—and there may be no more than 20 that eventually succeed."

If you are still keen on investing in new issues, wait for a slack year and stick to issues from large underwriters. And look at the fundamentals. Calculate how the prospect is priced relative to its sales and earnings, and make comparative calculations for other firms in its industry.

Somebody out there isn't doing the arithmetic. Ventritex Inc., a manufacturer of implantable heart defibrillators, was offered on Jan. 22, at 18, in an $84 million deal underwritten by Robertson, Stephens. At its current price of 19¼, Ventritex has an astronomical price/sales ratio of 44.

Our survey covered all new issues between Jan. 1, 1982 and Apr. 30, 1992 except foreign stocks, blind pools, limited partnerships, closed-end funds, real estate investment trusts and, as explained before, penny stocks. To avoid double counting, we credited only a single lead underwriter for each new issue.

Are you looking for cheap stocks in a rather expensive market? Precisely because everyone is sour on them, some defense stocks are good buys now.

# Swords into plowshares

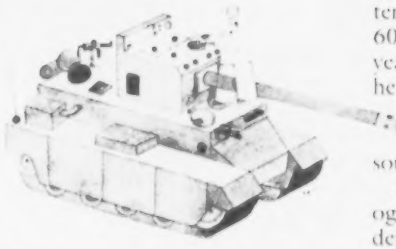
By Reed Abelson

THE GULF WAR is long over, and the politicians are vying with one another to grab money from the defense budget to spend on their favorite programs. No wonder defense stocks are in the dumps.

Which may make them an excellent buy for investors who are willing to buck the conventional wisdom. You don't have to believe in a full-scale resumption of the cold war to want to own these out-of-favor companies. Don't forget that many of them have civilian business, too.

Ah, but perhaps you have a long memory and recall how badly many defense outfits were burned after World War II and Vietnam when they tried to break into commercial markets. Thus it was that General Dynamics flopped in its effort to run Cessna Aircraft and Grumman discovered that making buses is very different from manufacturing military aircraft.

But people can learn from history,



and some defense firms certainly have. Anthony Marolda, president of the Winbridge Group, a Cambridge, Mass. consulting firm, says things are different this time. He says some defense contractors aren't merely making diversifying acquisitions for the sake of diversifying; instead, they are trying to adapt military technologies they already own to products that could be sold to other government agencies or commercial users. Many of the firms realize they don't know how to sell in commercial markets, so they have bought companies that know the commercial markets, formed joint ventures or acted as subcontractors to commercial businesses.

The classic model for this sort of move is Raytheon's 1965 purchase of an appliance manufacturer, Amana, in order to create a market for the technology behind the microwave oven.

The table below lists ten diversifying military suppliers. Some, like Raytheon and EG&G, are old hands at selling their stuff commercially. For others, like E-Systems and tiny Datametrics, diversification is a relatively new, and unproven, task.

E-Systems and Datametrics get the majority of their revenues from defense-related work, but they are determined to cut the military to under 60% of revenues within the next few years. Litton Industries has invested heavily over the last few years in its nondefense businesses of industrial automation and resource exploration.

How easily can a military technology be applied to civilian business? It depends. There's no commercial use for General Dynamics' nuclear submarines. But aviation electronics is just as important to commercial aircraft as to fighters, a fact long exploited by Rockwell International's Collins division. Satellites are extremely useful for nonmilitary work, as Martin Marietta, Loral and Hughes Electronics can tell you. Litton sells its navigation technology for use on long commercial flights. Datametrics, which sells color printers for use in military installations, is developing high-speed color printers for use wherever conditions are rough, like oilfields.

Defense companies are also realiz-

## Diversification as a defensive play

| Company | Recent price | 1991 revenues ($mil) | 1991 revenues % nondefense | Earnings per share 1991 | Earnings per share 1992 estimate | P/E on 1992 estimate | 5-year EPS growth rate |
|---|---|---|---|---|---|---|---|
| Datametrics | 1⅝ | $21 | 4% | $0.13 | NA | NA | NA |
| EG&G | 24¼ | 2,689 | 36[2] | 1.45 | $1.59 | 15.4 | 10% |
| E-Systems | 36 | 1,991 | 2 | 3.35 | 3.73 | 9.7 | 14 |
| GM Hughes | 20½ | 11,541 | 54 | 1.30 | 1.76 | 11.6 | 13 |
| Litton | 45⅝ | 5,219 | 48 | 1.45 | 4.09 | 11.1 | –6 |
| Loral | 31⅝ | 2,882[1] | 20 | 4.00 | 4.36 | 7.3 | 9 |
| Martin Marietta | 52⅜ | 6,075 | 28 | 7.08 | 7.41 | 7.1 | 11 |
| Raytheon | 44⅜ | 9,274 | 50 | 4.47 | 4.83 | 9.2 | 10 |
| Rockwell | 24 | 11,927 | 60 | 2.50 | 2.15 | 11.2 | –1 |
| Tech-Sym | 13 | 176 | 59 | 1.50 | 1.68 | 7.7 | 2 |

NA: Not available. [1]Fiscal year ended Mar. 31. [2]Does not include Department of Energy. *Sources: Forbes; Institutional Brokers Estimate System.*

**All these firms are making tactical forays into commercial fields where they can make use of their military technology.**

ing that they can find markets at other government agencies. Martin Marietta is providing the data processing skills it developed for the military to the Department of Housing & Urban Development. The company also developed robotics to handle radioactive weapons parts; it is adapting that technology in a contract to help the U.S. Department of Energy with hazardous waste handling. EG&G is taking its experience in operating two nuclear weapons factories and four other plants for the Department of Energy to the National Aeronautics & Space Administration and other agencies.

Even the most promising technologies, of course, won't transform a multibillion-dollar defense company into something else overnight. The $100 million or so in civilian sales that E-Systems might get this year from computer-based systems developed for the military "will get lost in the mass of the company," notes Michael Lauer, an analyst at Kidder, Peabody. Smaller companies such as Datametrics and Tech-Sym may have an easier time reinventing themselves.

Here's the point: In a market selling at 25 times earnings and having a 1.2 price/sales ratio, defense stocks sell for 11 times earnings, with a price/sales ratio of 0.56. But they are not going out of business. There's good reason to think the stock market has overreacted to their problems. So what's new? Markets usually do that.

Defense work is not going to disappear overnight. Anyone who thinks it is hasn't been watching TV. There are small wars today in the Balkans, the nations of the old Soviet Union are growling at each other, and some particularly slimy dictators rule such countries as Syria, Libya and Iraq.

And even without these threats, the Department of Defense is having a devil of a time eliminating some submarine contracts, because congressmen are protecting defense jobs. For example, that once-famous dove, Senator Christopher Dodd of Connecticut, has turned into a tiger in defense of the Seawolf submarine contract, which provides thousands of jobs in his state.

Between beating their swords into plowshares and continuing to build swords, defense companies will be around well into the next century. ■

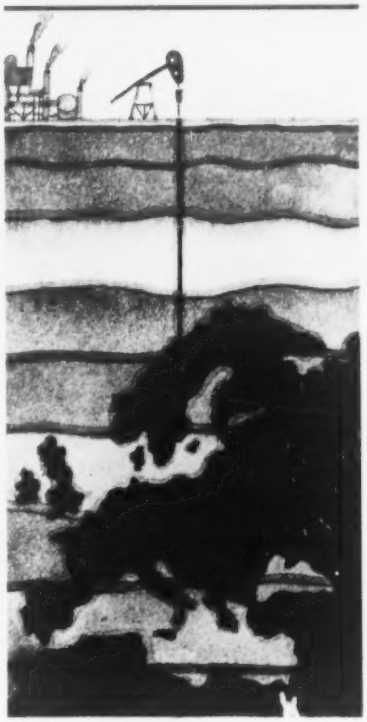
Want to play the possibility of higher oil prices? Consider buying shares of foreign-based petroleum companies.

# Exploring for oil stocks overseas

By Toni Mack

WITH THE SAUDIS apparently changing their minds about petroleum prices recently, a lot of people are taking a new look at oil stocks. Market laggards last year, the stocks have come to life in the last two months.

If you are tempted, says Kidder, Peabody analyst Bernard Picchi, buy the stocks of foreign oil companies as well as U.S. ones. Picchi has followed the industry for 15 years. He's logged a lot of air miles lately getting to know some European oil companies that trade at lower P/Es and stand to grow faster than their U.S.-based counterparts. Most of the European companies will raise their dividends this year, and many are available via American Depositary Receipts or Shares on the New York Stock Exchange.



Maybe you feel more secure buying known names—Texaco, say, or Mobil—than Elf Aquitaine. But Picchi reminds you that not so many years ago most U.S. investors were unfamiliar with the Royal Dutch/Shell Group, now the world's largest oil company. In the mid-1970s shares in Royal Dutch Petroleum languished on the New York Stock Exchange at four times earnings, a little more than a third of the market multiple. If you'd bought then and reinvested the dividends, you would now have three times as much money as someone buying the S&P 500.

The companies in the table on page 186 are ripe for discovery by U.S. investors, Picchi thinks. He notes that all the big oil companies are taking cash from U.S. operations and investing it abroad. Picchi believes that equity investors will follow, searching for foreign prospects.

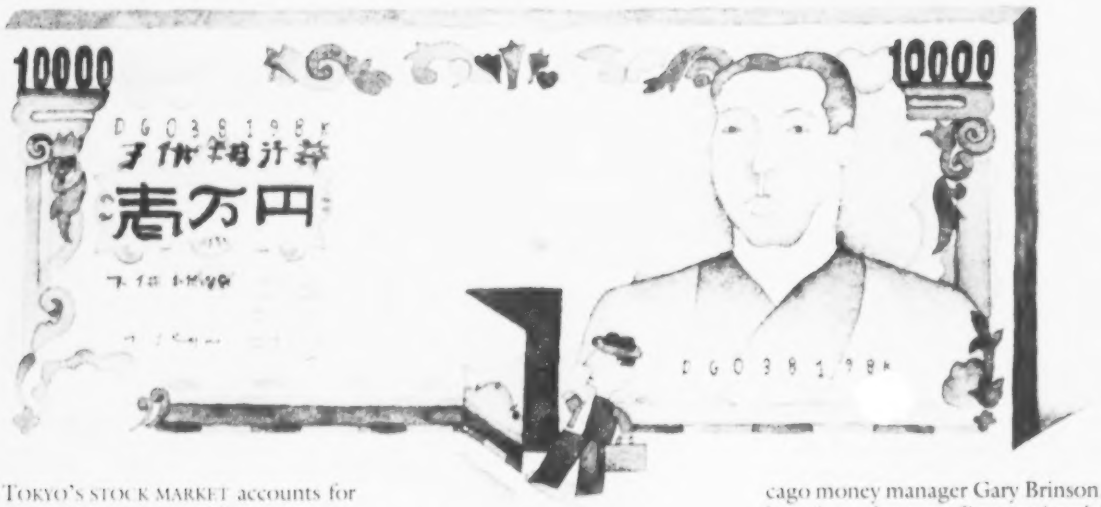
Repsol, a Spanish refiner and marketer, sells for 11 times expected 1992 earnings, at the low end of what U.S. refiners fetch. But while the domestic boys suffer massive environmental costs and little, if any, market growth, the Spanish gasoline market is growing 4% to 5% annually in unit volume. Repsol's earnings could swell an average 15% annually for the next five years, Picchi says.

Repsol is spending hugely—some $2 billion through 1995—but much of this outlay will enable the company

Japan Inc. is not going bust. With the Tokyo market still a smoldering ruin, now's a good time to pick up some bargains there.

# Toyota or Ford?

By Christopher Palmeri




TOKYO'S STOCK MARKET accounts for about 25% of the world's equity capitalization. If you don't have any of your assets in that market, you're probably making a mistake.

Oh, sure, the Japanese economy is slowing. Many Japanese companies are expected to report down earnings for the 1991 fiscal year, which ended in March; one of the best known of them, Sony, just reported a quarterly loss. The Japanese real estate and banking sectors have yet to see bottom. There could develop another selling panic, sending the Nikkei average down another 20%. Some pundits who shouted "buy" when the Nikkei sank to 20,000 saw it plunge another 15% or 20% before rallying.

Nevertheless, at 18,000, the index is still off more than 50% from its late 1989 high. This is an even worse collapse than that suffered by the U.S. markets in 1973-74, when they gave up around 40% of their value—before turning around and sextupling in the ensuing 18 years.

There are reasons to avoid Japan in the short term, but most of these are already reflected in stock prices. It took the U.S. market a long time to recover from the 1974 debacle, but when it did, long-term investors reaped riches. Japan could be a similar case. We're not talking this year or next year but about the money you are saving now to spend in retirement 20 or 30 or 40 years hence.

The Japanese market has been in a state of turmoil for the past month. One day the market is given over to a stampede by panicky sellers, sending the average down 3%; the next day the market spikes up 3%. It seems that a lot of buyers with cash to spend are waiting on the sidelines for the opportune moment.

A fair amount of such patient money—more than $5 million a week—is flying into the Japan Fund, managed in New York City by Scudder, Stevens & Clark. "We don't know if the market has hit bottom yet," says manager Elizabeth Allan. "But we think that long-term investors using dollar-cost averaging over the next six months should do very well."

Those thoughts are echoed by Chicago money manager Gary Brinson, a longtime advocate of international diversification, whose Brinson Partners manages some $22 billion. "If your Japanese exposure is zero, you should definitely look at this as an opportunity to build up a presence," he says.

Roger Ibbotson is a highly respected finance professor at Yale and president of the Chicago-based market strategy firm Ibbotson Associates. He says the Nikkei's three-year decline has put Japanese stocks roughly on par, by some measures, with U.S. equities. The market's price/earnings ratio is still high at 28, but the price/book ratio of 1.8 and the price/cash flow ratio of 8.6 are both lower numbers. (Here, cash flow is earnings plus depreciation.) Corresponding ratios in the U.S.: a price/book of 2.3 and a price/cash flow of 10.3.

So what then is the difference between Toyota and Ford? "Toyota has a better balance sheet," jokes Ralph Wanger, manager of the highly successful Acorn Fund.

If you want to get a piece of Japan, either an international mutual fund or an assortment of American Deposi-

## Brand names for less

| Company/business | ADR price ($US)[1] | 3-yr high | Price/ cash flow | EPS 1991 | EPS 1992E | Ordinary shares per ADR |
|---|---|---|---|---|---|---|
| **Canon**/office equipment, photography | $54.63 | $69.50 | 8.0 | $2.43 | $2.63 | 5 |
| **Dainippon Ink & Chemicals**/chemicals | 37.46 | 72.21 | 8.1 | 0.49E | 0.56 | 10 |
| **Fujitsu Ltd**/computers | 26.12 | 60.59 | 4.2 | 0.25 | 0.47 | 5 |
| **Hitachi Ltd**/semiconductors, electronics | 63.50 | 145.00 | 4.1 | 2.78 | 2.97 | 10 |
| **Hitachi Metals**/steel | 61.54 | 138.55 | 7.8 | 1.89 | 2.45 | 10 |
| **Honda Motor Co Ltd**/automobiles | 23.38 | 37.50 | 5.6 | 1.00 | 1.05 | 2 |
| **Matsushita Electric Industrial**/consumer electronics | 106.50 | 219.00 | 7.0 | 4.57 | 4.81 | 10 |
| **Mitsubishi Electric Corp**/industrial electronics | 38.39 | 87.63 | 4.3 | 1.20 | 1.28 | 10 |
| **NEC Corp**/computers | 38.00 | 91.88 | 5.2 | 0.37 | 0.82 | 5 |
| **Nippondenso Co Ltd**/automotive components | 45.20 | 76.66 | 7.3 | 2.19 | 2.02 | 4 |
| **Nissan Motor Co Ltd**/automobiles | 9.38 | 23.65 | 5.1 | 0.61 | 0.25 | 2 |
| **Ricoh Co Ltd**/office equipment, photography | 18.96 | 49.15 | 5.1 | 0.12 | -0.13 | 5 |
| **Sony Corp**/consumer electronics | 33.00 | 59.75 | 4.3 | 2.20 | 1.26 | 1 |
| **Toyota Motor Corp**/automobiles | 22.88 | 41.43 | 6.8 | 1.86 | 1.18 | 2 |
| **Victor Co of Japan Ltd**/consumer electronics | 14.55 | 42.73 | 4.7 | 0.12 | -0.13 | 2 |

[1] Equivalent price if recent ADR quote not available. E: Estimate.

*Sources: Morgan Stanley Capital International Perspective; Institutional Brokers Estimate System; Forbes.*

## Eastern exposure

| Fund | Total return 3-year* | Total return 1-year | Annual expenses per $100 | Assets ($mil) | % of assets in Japan |
|---|---|---|---|---|---|
| **International Equity** | 3.3% | -1.5% | $1.07 | $141 | 25% |
| **Japan Fund** | -6.6 | -25.9 | 1.26 | 340 | 84 |
| **Nomura Pacific Basin** | -0.1 | -17.4 | 1.48 | 45 | 70 |
| **Vanguard World Intl Growth** | 3.2 | -4.1 | 0.52 | 931 | 25 |

*Annualized. Returns through Apr. 30.

*Source: Morningstar, Inc.*

**Don't be put off by the weak recent performance of these funds with Japanese stocks in their portfolios. They did poorly precisely because Japanese stocks got cheap and are a buy now.**

tary Receipts *(see tables above)* is the way to do it. Consider investing half your target sum now and half a year from now. Don't be surprised if the market drops further.

ADRs are receipts for Japanese shares that trade like U.S. stocks on our exchanges. Since the average Japanese share trades at the equivalent of $7, low by U.S. standards, most ADRs are set up to be worth several Japanese shares.

ADRs and mutual funds are very much the way to go. Buying Japanese stocks directly creates a number of additional worries. Did you get a fair price for your trade? What additional charges—like custodial fees to hold the securities in Japan—will you have to pay? What will it cost you to convert your yen dividends into dollars? Will you get timely information on your company?

The round lot in Japan is 1,000 shares, so you will have to buy at least that many. Commissions on the Tokyo Stock Exchange are fixed at about 1.2% for smaller orders, but you can expect to pay more to the U.S. broker that handles your order. Merrill Lynch, for example, will charge 1.7% on its minimum $25,000 Japanese trade. Forget the U.S. offices of Japanese brokerage firms; they cater only to institutional investors.

Can you get the information you need about your Japanese holdings? Yes. Buying through a full-service broker like Merrill or Shearson will help. These and other full-service brokers maintain offices and analysts in Japan. Merrill is way ahead with a number of quarterly and monthly publications with information on specific stocks. Merrill's quarterly ADR review is a good start. Of course, these reports go only to customers with significant account balances. "A couple of hundred ADRs won't cut it," says Mauricio Rodriguez, a Merrill Lynch broker with a number of international accounts.

Don't hold your breath waiting for quarterly reports. "Japanese companies are only required to report the way they do at home, twice a year," says John Meserve, an ADR specialist at the Bank of New York. The 100 or so Japanese companies that offer ADRs provide sketchy quarterly announcements, plus annuals, in English.

Another excellent source of data: *Morningstar Japan*, a biweekly investment letter, in the style of Value Line, that covers 700 equities. It's available for $395 a year from Morningstar's

Chicago office. Or get the *Japan Company Handbook*, published by Toyo Keizai Inc. in New York City. Its two volumes, published quarterly, cover nearly 2,800 companies. The first volume covers what's called the first section in Japan, roughly akin to the New York Stock Exchange. The second volume covers regional and over-the-counter exchanges. Each volume is $55. Also try your target company's 20F filing, a report similar to a U.S. corporation's 10K that the Securities & Exchange Commission requires of every foreign company. Try the company's U.S. headquarters, your broker or one of the services that sell SEC documents. "You'll see information on market share and competition in detail you won't see in Japanese reports," notes Donald Krueger, a global strategist with the Templeton Funds.

What about dividends? They are subject to a 15% withholding tax by Japan. The withholding can generally be credited dollar for dollar against your U.S. tax bill, so it effectively doesn't cost you anything. Investors in mutual funds can often escape this hassle. Those in ADRs cannot. In any case, most Japanese companies make tiny payouts, preferring to reinvest in their business or in shares of other companies with which they are friendly. Thus, if your investment pays off, it will pay off largely in the form of a capital gain. Japan will not tax your capital gains, but of course the IRS will demand its cut of gains earned by U.S. residents.

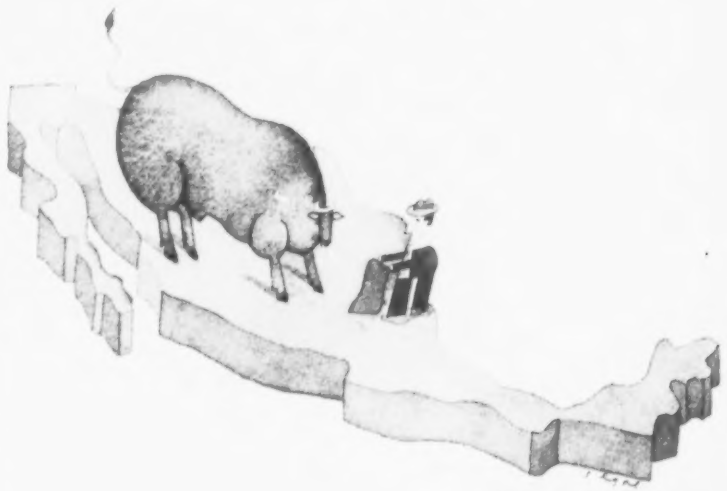
For a list of promising ADRs, we asked Morgan Stanley Capital International to search its database for companies with cash flow growth greater than the national average over the last four years (which came to 9% annually) and prices below the market's average multiple of 8.6 times cash flow.

Our table of funds consists of those no-loads with significant Japanese holdings and the lowest expense ratios. You can also put some weight on performance. But don't choose a Pacific Basin fund simply because it beat some other Pacific Basin fund in recent years. The best performers, by this measure, are the ones with the lowest Japanese exposure. That's the reverse of what you want. ■

Mexico is an economic miracle but a long since discovered miracle. Some of the smart money is already taking its profits on the Bolsa.

# Too late?

By Claire Poole



FIVE YEARS AGO, when Mexico was given up for dead by U.S. investors, Teléfonos de Mexico traded over-the-counter at 2½ for each of the company's current NYSE-traded American Depositary Shares. Now everyone wants in on Mexico. Telmex, whose shares went on the Big Board a year ago at 27¼, has since doubled to a recent 56⅞.

Thus with the whole Mexican market. In late March the Index of Prices & Quotes, Mexico's version of the Dow Jones industrial average, topped 1900 before stabilizing recently near 1840; five years ago the index was at an inflation-adjusted 140. With its market capitalization surpassing $140 billion, the Mexican Bolsa is now the ninth-largest market in the world.

No surprise that Mexican companies are taking advantage of the new popularity of their market to raise money in the U.S. At least 20 Mexican companies now traded only in pesos or privately held are expected to tap overeager buyers in the U.S. by raising U.S. dollars via ADR offerings or private placements. *(For a sample, see table, p. 198.)* The new companies would join 20 others that already have stock trading in the U.S.

If your broker offers them to you, tread warily. The Bolsa's price/earnings ratio now averages 15—versus 12 just a year ago. At that level, equities are almost as expensive in Mexico as in the U.S.—which is by no means cheap at current levels. (The S&P 500 is trading at 18 times inflation-adjusted averaged earnings over the last five years.)

Analysts who follow Mexican stocks are loath to say bluntly that the market is overheated, but they will hint in that direction by saying that it is becoming more selective, meaning you have to be very lucky to get a stock that goes up.

A few things to remember:

## The Mexican flood

| Company/business | 1991 sales ($mil) | 1991 earnings ($mil) | Recent price ($US) | P/E | Price/ book value | Yield |
|---|---|---|---|---|---|---|
| **Apasco**/cement | $326 | $52 | $3.50 | 16.2 | 140% | 0.6% |
| **Arka**/brokerage | 34 | 8 | 2.03 | 6.2 | 140 | 0.6 |
| **Banacci-CCP**/financial services | 2,148E | 516E | 6.49 | 15.0 | 170 | 0.0 |
| **Comercial Mexicana**/supermarkets | 1,417 | 68 | 1.31 | 17.2 | 230 | 0.7 |
| **Desc**/diversified | 1,593 | 66 | 3.36 | 11.2 | 110 | 2.9 |
| **GBM-Atla**/financial services | 307E | 50E | 4.54 | 23.0 | 110 | 0.0 |
| **Gemex**/beverages | 287 | 30 | 8.23 | 21.3 | 530 | 0.0 |
| **Grupo Mexico**/mining | 911 | 38 | 2.50 | 19.1 | 60 | 0.0 |
| **Maseca**/tortillas | 357 | 40 | 0.79 | 16.0 | 340 | 2.5 |
| **Nadro**/drugstores | 550 | 18 | 14.98 | 14.8 | 450 | 0.8 |
| **Quadrum**/transportation | 51 | 5 | 5.15 | 9.2 | 140 | 0.0 |
| **Sanborn**/retailing | 323 | 26 | 3.55 | 19.0 | 160 | 0.0 |
| **Serfin-Obsa**/financial services | 1,271E | 156E | 0.45 | 19.4 | 130 | 0.0 |
| **Soriana**/supermarkets | 539 | 26 | 3.20 | 13.6 | 120 | 0.0 |
| **Synkro**/consumer products | 183 | 21 | 2.10 | 10.8 | 160 | 0.0 |

Prices as of May 20. E: Estimate.
*Sources: Acciones y Valores; Forbes.*

**Make way for offerings from south of the border. Here's a sampling of those that already trade on the Mexican Bolsa and may appear in the U.S. as ADRs.**

Despite its recent strength, the Bolsa is not as liquid as U.S. markets and is even more volatile. Liquidity? Around 70% of the trading takes place in just 20 of the 200 companies listed. Telmex so dominates the Bolsa that news, either good or bad, on this stock can move the entire market. In early March the Bolsa dropped sharply after the Mexican government's announcement that it was planning to place another 5% of Telmex shares in the stock market.

Volatility? Tubos de Acero de Mexico, or Tamsa, is a big producer of seamless steel pipe for the petroleum industry. Last October this company sold 4 million shares outside Mexico at 10¼ in an offering led by First Boston and Obsa International. The stock got as high as 11¼ on the American Stock Exchange, then skidded in early April to 5¼, its lowest level in almost two years. What happened? After reporting one of its best years yet, Tamsa announced that deteriorating exports, which make up half of the company's sales, would seriously affect 1992 results. It's now trading at 6⅛, or eight times earnings.

Those who bought Vitro, the $3 billion Monterrey glassmaker and Mexico's largest industrial conglomerate, weren't much luckier. Vitro sold 6.5 million shares on the Big Board last November at 25⅜ in an offering led by First Boston. After rising to as high as 32¼ in March, the stock dropped to 21⅝, taking the Bolsa with it. Why? Worse-than-expected news that Vitro's net earnings had fallen nearly 20% in 1991 because of debt refinancing costs and higher income taxes. The stock is still down at around 23¼.

Cementos Mexicanos, more commonly known as Cemex, is a $1.7 billion cement producer, the largest in North America and fourth largest in the world. It wanted to raise $1.2 billion in an international stock offering to pay down debt. When investors balked, Cemex's underwriters, led by Morgan Stanley, chopped the offering in half, and ended up selling the stock in April at a 6% discount. The shares are hovering around the offering price of 56,200 pesos ($18) on the Mexican Bolsa; this one is not yet available as an ADR.

What stocks are being packaged for export to Americans? Grupo Desc is one of them. Mexico's fifth-largest industrial group, with $1.6 billion in sales, it plans a $300 million offering sometime this summer, and is trading at 1.1 times book and 11 times earnings. The company, however, is suffering. While its real estate and auto parts divisions are profitable, Desc desperately needs to sell off unprofitable divisions like petrochemicals and dump unrelated divisions like poultry. Last year Desc reported earnings of $66 million—a 20% drop from the previous year—on flat sales. Do you really want to pay 11 times earnings for something whose earnings are going down?

In the industrial sector, it's probably better to stick with the cement and construction companies. Luis Martínez, analyst with Inverlat in Mexico City, likes Cementos de Chihuahua, a privately held subsidiary of Cemex that dominates Mexico's fast-growing Northwest cement market. Cementos de Chihuahua is planning a $130 million initial public offering sometime this year to finance construction of an 850,000-ton cement plant near the border towns of Ciudad Juárez and El Paso.

Hermann von Bertrab, analyst with Arka Securities in La Jolla, Calif., likes $326 million (sales) Apasco, the fourth-largest cement producer in Mexico, controlled by the Switzerland-based Holderbank. Apasco has been taking business away from Cemex, he says, and is better financed. Apasco is also considering an offering.

A handful of Mexican supermarkets are headed for the international markets this year. One is the $1.4 billion (sales) Comercial Mexicana, the third-largest and most profitable supermarket chain in Mexico. Comercial has hooked up with Price Co. to build warehouse clubs in Mexico, the first of which opened in February and is already exceeding its sales goals.

Another is Soriana. The $540 million (sales) supermarket chain, with stores mostly in northern Mexico, hasn't yet hooked up with an American retailer. It's now facing competition from Cifra, which plans to enter Soriana's northern markets this year with its Wal-Mart-inspired discount clubs. Soriana's sales were already flat last year.

Among specialty retailers, Nomura Research Institute's Jorge Suárez likes Nacional de Drogas, or Nadro, Mexico's largest drugstore chain, with $550 million in sales. He also likes Sanborn, the $323 million (sales) combination five-and-dime/coffee-shop chain controlled by Telmex's Carlos Slim. Both are talking about international offerings.

Several Mexican financial groups will be looking for international financing this year and next, hoping to repeat Grupo Financiero Bancomer's $837 million private placement in March by J.P. Morgan. Nomura's Suárez likes Banacci, which consists of recently privatized Banamex, Mexico's largest bank, and Acciones y Valores, Mexico's top brokerage firm (FORBES, *Mar. 30*). He also likes Operadora de Bolsa, or Obsa, Mexico's largest retail brokerage firm, which recently bought Banca Serfin. He recommends avoiding smaller offerings like Arka and Prime, both brokerage firms that haven't hooked up with banks but may have offerings in the next year.

When the public gets into a market, the early birds often get out. There are signs this is happening in Mexico. In April short-selling became legal in Mexico for the first time. That highly successful investor Paul Tudor Jones is said to be shorting Mexican stocks. The fabled George Soros has cut back on his Mexico holdings.

Our advice: Wait for a good reaction before making any major commitments to Mexican stocks.

Right now European stocks look a lot cheaper than U.S. stocks. Here's a smart way to play Europe.

# Europe at 15% off

By Suzanne Oliver

BY ALMOST ANY conventional measure, U.S. equities are expensive today. Nearly every market in Europe is cheaper than the U.S. stock market in price to book value, price to cash flow and price to earnings.

Investors who look for value rather than hot trends would be smart to consider European stocks right now. Most of Europe is in a recession. So was the U.S. during 1991, when the S&P 500 gained 30%. That rally was fueled by falling interest rates and anticipation of an economic rebound.

Mark Edwards, a manager of the T. Rowe Price European Stock Fund, expects the same thing to occur in Europe. Recently the U.K. and France cut interest rates slightly. "The Bundesbank may not ease significantly until the first quarter of 1993," says Edwards. "But if people start to sniff interest rate easing, the markets could take off."

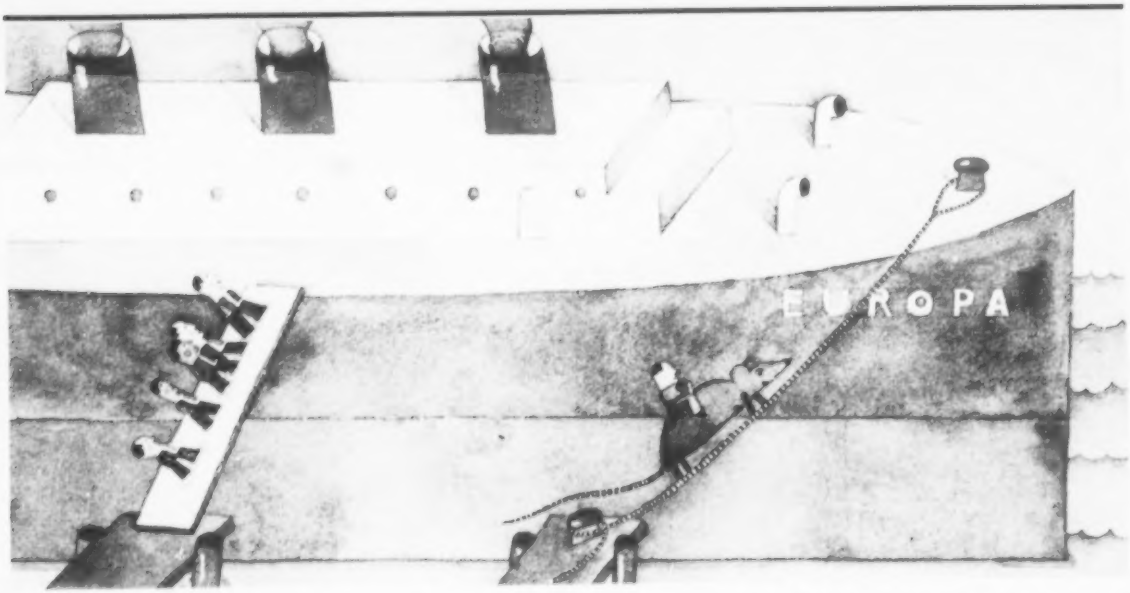
How to play the prospective recovery? You can spend a lot of time learning about European companies or you can buy a good no-load fund and let someone else do the tough job of selection for you. Investors looking for no-load mutual funds do not have many choices. There is the T. Rowe Price European Stock Fund, up 9% in the past 12 months, or the Vanguard International Equity Index Fund European Portfolio, up 11%. The Van-

## Discount fares

| Fund | Assets ($mil) | Discount | Annual expenses per $100 | Yield |
|---|---|---|---|---|
| Austria | $80 | 7.2% | $1.68 | 0.0% |
| Emerging Germany | 126 | 16.1 | 1.70 | 3.1 |
| Europe | 102 | 8.4 | 1.58 | 3.0 |
| France Growth | 127 | 13.0 | 2.14 | 2.6 |
| Future Germany | 179 | 13.8 | 1.29 | 0.0 |
| Growth Fund of Spain | 203 | 13.5 | 1.23 | 1.5 |
| GT Greater Europe | 178 | 14.2 | 1.87 | 1.2 |
| Irish Investment | 46 | 16.2 | 1.69 | 5.5 |
| Italy | 64 | 15.6 | 1.62 | 3.7 |
| New Germany | 354 | 13.7 | 1.13 | 0.0 |
| Scudder New Europe | 157 | 11.1 | 1.85 | 5.7 |
| Spain | 119 | 6.9 | 1.98 | 1.6 |
| United Kingdom | 40 | 14.4 | 1.88 | 6.6 |

Assets as of Mar. 31. Yield on market price as of Apr. 30. Cash flow is earnings plus depreciation.
NA: Not available or not applicable.
*Sources: Morningstar, Inc.; Morgan Stanley Capital International Perspective; Forbes.*

**Closed-end funds selling at less than their asset values are a cheap way to get to Europe.**




guard fund tracks an index of about 600 stocks from 13 European countries. It has a very attractive expense ratio of only 0.33% (33 cents a year for every $100 you invest). That low ratio is one fifth the average for international funds.

But for more venturesome investors there's a cheaper way to buy Europe today: through closed-end funds. These trade on stock exchanges at prices that can be more or less than their asset values, depending on demand. Currently most European closed-ends are trading at wide discounts to their asset values.

You can get the France Growth Fund at a 13% discount to its net asset value. In the latest 12 months the fund has lagged the French market's 24% rise. That is because fund manager Philippe Cartier has moved the fund into cyclical and interest-rate-sensitive stocks, but the recent rally favored growth stocks instead. The United Kingdom Fund, at a 14% discount, also has weightings in cyclical stocks. Since John Major was reelected, the U.K. market has rallied, but Edwards thinks earnings won't turn up until next year.

Three heavily discounted closed-end funds invest in Germany. Emerging Germany and New Germany Funds invest in small and medium-capitalization stocks. Future Germany holds mostly German blue chips and is a clone of the better-known Germany Fund. Germany and Future Germany are managed by Deutsche Bank's John Abbink, but Germany trades at a 3% discount, while Future Germany has a 14% discount.

The Spanish stock market is down this year, and the three-year-old premium on the Spain Fund has finally dropped to a discount. Still, the larger Growth Fund of Spain is a better buy. Besides outperforming Spain Fund since its 1990 debut, Growth Fund of Spain has a bigger discount and a lower expense ratio than does the Spain Fund.

Italian stocks are Europe's cheapest relative to their book values and cash flows. Those low valuations reflect a lack of confidence in the Italian government and the Italian economy; if you are more sanguine, buy the Italy Fund, managed by Shearson Lehman Global Asset Management. The fund, currently trading at a 16% discount to its net asset value, has had only one up year since its 1986 beginning.

The table opposite lists 13 closed-end funds trading at discounts of 6% or more. You can buy a diversified fund such as the Europe Fund or assemble your own basket of assorted country funds. If your time horizon is short, you are better off at the Vanguard or T. Rowe Price no-loads, where expense ratios are low and you are assured of being able to exit at full net asset value. ■

**By three significant measures, European stocks are cheaper than U.S. stocks.** ■

## What markets cost

| Country | Price/ book value | Price/ cash flow | Price/ earnings |
|---|---|---|---|
| Austria | 169% | 4.7 | 27.7 |
| France | 168 | 6.9 | 15.6 |
| Germany | 192 | 4.9 | 16.7 |
| Ireland | 157 | 9.7 | 14.3 |
| Italy | 110 | 2.6 | 14.9 |
| Spain | 119 | 4.8 | 10.0 |
| UK | 200 | 9.4 | 16.7 |
| US | 228 | 10.3 | 23.8 |

Based on prices as of Apr. 30.
*Source: Morgan Stanley Capital International Perspective.*

You can make a very good return investing in Latin American debt. Here's how to size up the risks and the rewards.

# Looking south for better yields

By Joel Millman

MEXICO, Argentina, Chile and even Venezuela and Colombia are getting their economies back into shape. Borrowers, both corporate and governmental, have the wherewithal to repay dollar debts; even local-currency bonds are turning in good returns for foreign holders.

Short-term government bonds payable in Mexican pesos, for instance, offer a healthy 12.8% coupon, yet the peso has depreciated only 2.7% against the U.S. dollar over the past year. If the peso maintains that kind of strength, a U.S. buyer will net 10%, not bad for short-term debt at a time when U.S. Treasury bills earn but 4%.

Of course, there is no such thing as a risk-free 10% return. If you want to get a piece of the action south of the border, stop long enough to reflect on what has happened to some of the investors who went before you. Cuban bonds were once thought solid, pre-Castro. U.S. banks had to write off tens of billions in Latin loans in the 1980s. In 1982 Mexico forcibly converted dollar deposits at unfavorable rates into rapidly depreciating pesos.

So what's different now? Latin America is finally turning away from socialism and its first cousin, statism. State enterprises are being privatized, taxes are being collected and flight capital is returning in the billions of dollars. Inflation is down everywhere except Brazil.

U.S. investors who want to buy Latin debt cannot, unfortunately, get a pure dose of it through any SEC-registered fund, although many international bond funds have a portion of their assets in Latin America. But there are other alternatives.

One is to buy marketable government securities through a foreign broker. Don't waste your time with the big U.S. brokerage houses. So far they have been interested in buying these securities only for institutional investors. Discounter Charles Schwab simply doesn't handle foreign-currency debt.

A very accessible instrument for smaller investors is the Mexican equivalent of our T bill, called Cete (for Certificado de la Tesorería). Cetes paid rates as high as 24% (discount basis) early last year, and 16% at the beginning of 1992. Lately the rates have been holding steady at around 13%—still attractive in light of the peso's recent strength.

A one-year Cete for 100 million pesos (about $33,000) would cost you a markup of about $75 over its wholesale price. On top of this, you have a currency conversion cost, but the Mexican brokerage firms say this is minimal. Obsa, for example, says that it is willing to buy dollars at only 1 peso less than what it sells dollars for, on trades of $33,000. This equates to a round-trip conversion cost of only 0.05%. Markups and conversion spreads would nick your return on the Cete, but it would still be well above that available in the U.S. except on the junkiest of junk bonds.

Trader Roberto Verthelyi at Oppenheimer & Co. is a bull on Argentina. He has been touting BIC V's (for the fifth series of government Bonos de Inversión y Crecimiento), available in $100,000 chunks. The BIC V is a ten-year self-amortizing bond, with payments (in pesos) currently running at 2.85% of the bond's principal. Of this distribution, 2% is interest (for a compounded yield of 26%) and the rest a return of principal. Convert your monthly payout immediately, even though small trades are expensive in the currency market. Argentina has a law pegging the peso 1-to-1 to the dollar, but then, you never know.

Another option is to walk into a U.S. branch of a Latin bank and ask how to open a peso account with the home office. The bank may wire your dollars south, where they will be con-

## Stick with strong currencies

| Country | Short-term govt bond rates | Currency depreciation[1] |
|---|---|---|
| Argentina | 8.1% | –1.0% |
| Chile | 8.0 | –2.2 |
| Mexico | 12.8 | –2.7 |
| Venezuela | 38.0 | –15.9 |
| Brazil[2] | 924.0 | –90.1 |

[1]May 1991 to May 1992. [2]Annualized inflation adjusted, 19% per month. *Sources: Deltec Securities, International Finance Corp.*

**A 90.1% devaluation turns a 924% yield into a dollar return of 1.4%.**

verted into the local currency. Recent rates on foreign-currency bank CDs: Mexico, 12%; Argentina, 12%; Venezuela, 30% to 40%. Again, there is a haircut on your conversion. The bank will probably offer an attractive rate going into the peso—the banks are hungry for U.S. dollars—while offering a poorer deal when you want to turn your money back into dollars.

Taxes? There's no tax withholding by Mexico. Interest is, of course, taxable to U.S. residents. Currency losses incurred on a debt security are deductible as an ordinary loss, says Monica Sabo of Arthur Andersen's Chicago office.

The final option is to ask a foreign bank or brokerage for information about buying shares of a foreign-

**State enterprises are being privatized, taxes are being collected and flight capital is returning in the billions.**

operated fixed income mutual fund. Mexico's Bolsa de Valores, for example, carries more than 80 of these open-ended *rentas fijas*, most of them carrying loads of less than 1%. While the account must be opened in Mexico, that doesn't mean the investor has to present himself down there. U.S. offices of the biggest Mexican houses—Arka, Inverlat, Obsa, for example—are all equipped to put you in touch with the home office. The top performer, the Finreal fund sponsored by Inverlat, earned a total (peso) return of 33% last year, or 30% when converted back into dollars. Minimum account, $33,000.

Is it safe to play Latin debt for that extra yield? Not if you are betting grocery money. "The capital flows coming into the region right now are enormous, so it's a relatively safe bet," says Gerard Finneran, managing director of Trust Co. of the West, a highly regarded Los Angeles-based specialist in Latin debt restructurings. "But you have to know when it's time to get off the merry-go-round." Put it this way: The changes for the better in Latin America are probably irreversible, but the probability is a good way from 100%. ■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BY ERIC S. HARDY

Dean Witter investment strategist William Dodge is betting that in the long run low inflation will enable the economic recovery to sustain itself without any big jump in interest rates. Somewhat a contrarian, Dodge likes big department stores such as May, J.C. Penney and Dayton Hudson, and computer makers IBM, Apple and Dell. His software picks include Microsoft, Novell and Oracle Systems. One of his favorite stocks is pharmaceutical house Bristol Myers Squibb. It shows earnings growth and a dividend yield above the market averages, yet sells for a relatively low 18 times earnings.

Dodge, however, is not bullish on the market as a whole. He thinks it's quite overvalued with the Dow over 3400. The Barra All-US index of about 5,300 stocks sells for 28 times its latest 12 month earnings, nearly 2.4 times book value, and 36 times dividends. All these ratios are high by historical standards and are also high in relation to corresponding ratios in European countries *(see table, p. 201)*.

During the past two weeks the Dow industrials moved into new territory, but with a noticeable lack of enthusiasm. One of the hottest sectors of the market—new issues—may be running out of steam *(see p. 158)*.

A number of other market benchmarks look weak as well, including breadth (the number of advancing stocks to declining ones) and the daily ratio of new highs to new lows. One indicator that still is in positive territory: The Barra All-US index remains comfortably above its 200-day moving average. It has managed this even though the latest close on the All-US index is slightly below the Dec. 31, 1991 level.

The stocks of small companies perform spectacularly well on occasion—such as during most of 1991. But over the past five years, Barra, Inc. reports, an investment in ten-year corporate bonds not only returned as much as small-capitalization stocks but also imposed only about half as much risk on the investor.

## The overall market

## Closeup on the market

| Index or investment | 2-week change | % change from 1 year | % change from 5-year high |
|---|---|---|---|
| Barra All-US index | 0.6% | 8.5% | -2.9% |
| S&P/Barra Growth index | 1.4 | 10.8 | -4.7 |
| S&P/Barra Value index | 0.6 | 10.8 | -0.3 |
| Dow Jones industrials | 0.9 | 13.3 | 0.0 |
| S&P 500 | 0.9 | 7.7 | -1.0 |
| NYSE | 0.7 | 8.4 | -1.1 |
| Nasdaq | 0.7 | 15.4 | -10.0 |
| Amex | 0.1 | 6.1 | -6.4 |
| EAFE | 1.1 | -7.1 | -24.5 |
| CRB index[1] | 1.8 | -4.0 | -24.0 |
| Gold | 0.2 | -7.3 | -32.9 |
| Yen | 0.7 | -6.0 | -21.0 |
| Oil | 6.8 | 3.1 | -46.7 |

## The best and worst performing stocks[1]

| Best | Price | 2-week change | 1992 EPS[2] | Worst | Price | 2-week change | 1992 EPS[2] |
|---|---|---|---|---|---|---|---|
| First Florida Banks | 44 1/4 | 42% | $2.15 | Meridian Diagnostics | 10 5/8 | -29% | NA |
| System Software Assoc | 29 1/4 | 34 | 1.36 | Software Toolworks | 3 5/8 | -28 | $0.35 |
| Scios | 14 | 32 | -0.88 | Qual-Med | 14 1/4 | -25 | 1.50 |
| Puritan-Bennett | 34 1/4 | 32 | 1.16 | Centel | 31 7/8 | -24 | 0.69 |
| BJ Services | 15 1/4 | 28 | 0.94 | HMO America | 10 1/2 | -24 | 1.28 |

## The best and worst performing industry factors[1,2]

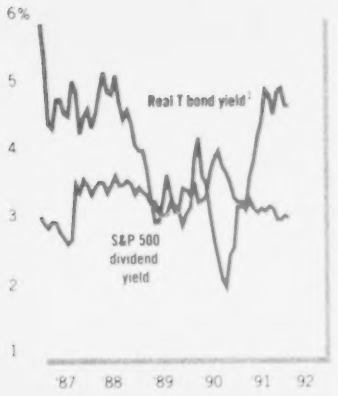
| Best | 2-week change | Since 12/31/91 | Worst | 2-week change | Since 12/31/91 |
|---|---|---|---|---|---|
| Oilfield services | 9.6% | 6.1% | Tire & rubber | -6.6% | 22.3% |
| Gas utilities | 5.5 | 1.5 | Air transport | -5.8 | -13.3 |
| International oil | 4.7 | -0.4 | Tobacco | -2.8 | 4.0 |
| Non-life insurance | 3.7 | 4.2 | Consumer durables | -2.2 | 14.2 |
| Aluminum | 2.6 | 2.7 | Telephone | -2.2 | -2.5 |

Note: Data for period ending 5/28/92. The Barra All-US index consists of all publicly traded common stocks for which price quotations are available and ordinary shares of foreign stocks trading on U.S. markets. ADRs, REITs and closed-end funds are excluded. [1] Total return of a portfolio of more than 150 large-capitalization stocks that has high historical earnings growth and has predicted above average earnings growth. [2] Total return of more than 300 large-capitalization stocks characterized by low price-to-book ratios, high yields and low price-to-earnings ratios. [1] A dollar-denominated capitalization-weighted index of more than 1,000 stocks from Europe, Australia, New Zealand and the Far East. Source: Morgan Stanley Capital International Perspective. [2] Index of 21 commodity futures. [1] Knight-Ridder Financial Information. [1] During the last two weeks. [2] Estimate. Source: Institutional Brokers Estimate System, from IBES, Inc. [1] Shows return to the industry factor after controlling for other influences including company size, value and growth characteristics. Multi-industry firms have proportional contributions in two or more groups. NA: Not available. Principal source: Barra, Inc., Berkeley, Calif.

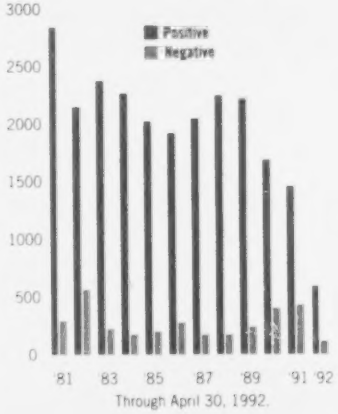
# DIVIDENDS REVIEW

BY GILBERT STEEDLEY

### Corporate vs. government yields




### Corporate dividend revisions




Through April 30, 1992.

Dividends have been going up, but not as fast as stock prices.

Arnold Kaufman, an economist at Standard & Poor's, predicts that close to 1,300 U.S. corporations will raise their dividends this year; only 1,086 did so last year. Kaufman expects that the composite dividend for the S&P 500 index will be $12.80 this year, up 5% from 1991. The 1991 figure was up less than 1% from 1990.

But stocks have raced ahead of these dividend gains. The S&P 500 index rose 6.5% over the past year. Thus the yield, 3%, is slightly lower than it was a year ago.

The table below left lists ten companies that are good candidates for increasing their dividends in the near future. These companies pay out less than 55% of net earnings on dividends. Standard Commercial, which sells tobacco, has raised its dividend in six out of the last ten years and is in good shape to raise it again.

The table at the bottom right shows companies with above-market yields. We searched for companies having a high ratio of earnings plus depreciation (where applicable) to capital expenditures plus dividends. These companies also have a B++ or higher financial rating from the Value Line Investment Survey.

### Representative industry yields

| Industry | Yield | Payout ratio[2] | P/E | Industry | Yield | Payout ratio[2] | P/E |
|---|---|---|---|---|---|---|---|
| Auto & truck mfg | 5.1% | NM | NM | Household prods | 2.5% | 40% | 25 |
| Banking | 4.2 | 44% | 16 | Integrated petroleum | 4.9 | 128 | 28 |
| Basic chemicals | 4.5 | 74 | 19 | Pharmaceuticals | 2.2 | 38 | 22 |
| Electric utilities | 6.6 | 107 | 16 | Retail | 2.0 | 38 | 23 |
| Electrical equipment | 3.0 | 40 | 14 | Telecommunications | 4.3 | 60 | 30 |

### Companies that may raise their dividends

| Company | Price | Indicated rate | Yield | Payout ratio | Trailing EPS |
|---|---|---|---|---|---|
| Centex | 42¼ | $0.40 | 0.9% | 18% | $2.21 |
| Crane | 27½ | 0.75 | 2.7 | 52 | 1.43 |
| Ecolab | 34½ | 0.70 | 2.0 | 34 | 2.03 |
| Hechinger | 9⅝ | 0.16 | 1.7 | 24 | 0.66 |
| IMC Fertilizer | 46⅞ | 1.08 | 2.3 | 21 | 5.06 |
| Intl Shipholding | 21¼ | 0.20 | 0.9 | 9 | 2.19 |
| EW Scripps | 28⅞ | 0.40 | 1.4 | 40 | 1.01 |
| Service Corp Intl | 27¼ | 0.56 | 2.1 | 37 | 1.51 |
| Standard Commercial | 27⅛ | 0.52 | 1.9 | 25 | 2.07 |
| VWR | 27⅛ | 0.80 | 2.9 | 53 | 1.51 |

### High-yielding stocks

| Company | Price | Indicated rate | Yield | Trailing EPS |
|---|---|---|---|---|
| Aetna Life & Casualty | 42⅞ | $2.76 | 6.4% | $5.22 |
| American General | 47⅛ | 2.08 | 4.4 | 4.46 |
| California Water | 32 | 1.86 | 5.8 | 2.45 |
| Cigna | 52 | 3.04 | 5.8 | 7.15 |
| Montana Power | 25⅜ | 1.54 | 6.1 | 1.99 |
| National Fuel Gas | 25⅛ | 1.46 | 5.8 | 1.89 |
| San Diego Gas & Elec | 23⅛ | 1.44 | 6.2 | 1.77 |
| So New Eng Telecom | 31¾ | 1.76 | 5.5 | 2.06 |
| Washington Gas Light | 35⅛ | 2.14 | 6.1 | 2.49 |
| Wisconsin Public Svcs | 27⅞ | 1.70 | 6.1 | 2.32 |

Note: All data, except where footnoted, as of 5/28/92. [1]Yield on 30-year Treasurys adjusted for inflation using the trailing 12 months' increase in the Consumer Price Index. [2]Capitalization-weighted. Dividends divided by net income; all extraordinary items are excluded. NM: Not meaningful. Sources: Media General, Value Line, via Lotus One Source; Standard & Poor's.